

**BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001**

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POSTAL RATE AND FEE CHANGES

Docket No. R2000-1

**Initial Brief Of
Major Mailers Association**

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Major Mailers Association ("MMA") hereby submits its initial brief. In this case, MMA has presented its case on First-Class Mail issues through the testimony and exhibits of three witnesses:

- ◆ Richard E. Bentley, an expert witness who has testified before this Commission in numerous rate and mail classification proceedings for over twenty years. TR 26/12273-12335. In addition, he sponsored Library Reference MMA-LR-1, which derives MMA's workshare unit cost savings.
- ◆ Sharon Harrison, the Technical Director, Billing Solutions Technology of SBC Services Inc. TR 26/12216-33. Ms. Harrison, who has over twenty years of experience in all aspects of mail operations for large telecommunications mailers, is responsible for SBC's overall relationship with the Postal Service.
- ◆ Mury Salls, Executive Vice President of AccuDocs, a large document processing company which mails more than 300 million statements, invoices, and other documents each year. TR 26/12260-67. Mr. Salls, the co-founder and President of MMA, previously testified before this Commission in Docket No. MC95-1.

Based on the testimony of its witnesses and the other record evidence discussed below, MMA respectfully requests that the Commission recommend modest increases of at least 0.2 cents and 0.3 cents, respectively, in the Basic Automation and 3-Digit Automation discounts, and that the 4.6 cent heavy weight discount be extended to First-Class workshare letters weighing between 1 and 2 ounces.

Statement Regarding MMA's Interest In This Proceeding

MMA is an association of quality First-Class Mailers, organized for the purpose of promoting fair and equitable postal rates, classifications, and rules. MMA has participated actively in all major rate and classification proceedings considered by the Commission over the past decade.

MMA members are among the largest mailers of "workshare" First-Class Mail that is presorted and prebarcoded. The Postal Service's rate and fee proposals in this proceeding directly affect MMA members' postage costs, their costs of mail preparation, and their postage discounts.

Overview Of The Postal Service's Proposals

In this case, the Postal Service has made several proposals that could adversely impact First-Class mailers in general and the members of MMA specifically. First, the Postal Service has proposed to increase the basic First-Class rate by one cent to 34 cents, to increase the rate for the second and subsequent ounces from 22 to 23 cents, and to increase the rates for workshare mail in real terms by maintaining the nominal discounts at current levels.¹

Second, the Postal Service claims that the contingency allowance should be raised from the 1 percent level approved by the Commission in Docket No. R97-1 to 2.5 percent. That proposal has a pervasive impact on all mailers.

Third, as it did in the last case, the Postal Service proposes to modify the long-established method of attributing costs to subclasses and services. Postal witnesses claim that labor costs, the major cost component, do not vary 100 percent with volume.

Finally, in presenting its case for higher rates, the Postal Service began with FY 1998 actual data. As a result, in the middle of this case the Commission ordered the Postal Service to provide updated base year information using final FY 1999 information that became available after its original filing.² MMA understands that the Commission embarked upon this updating process so that its recommended decision could reflect the most recent information. Perhaps some of that information will assist the Commission. However, much of the information produced by the Postal Service appears to have been interpreted in a manner that favors one of the Postal Service's long term goals -- shifting additional cost burdens from Commercial Standard mailers to First-Class mailers. As such, this more recent information is inherently unreliable and

1 The Postal Service is proposing to reduce the discount for First-Class Non-Automation Letters, from 2.5 to 2.0 cents.

2 See Order No. 1294, issued May 26, 2000. In response to Order No. 1294, the Presiding Officer issued POR 71 modifying the procedural schedule to permit receipt of this additional information.

ultimately prejudicial to MMA and other mailers because it was never subjected to the rigors of the discovery process.

Summary Of MMA's Proposals

In contrast to the Postal Service's hold-the-line approach to First-Class workshare discounts, MMA urges the Commission to recommend modest increases of at least .2 cents and .3 cents, respectively, in the Basic Automation and 3-Digit Automation discounts.³ MMA further requests that the Commission recommend that the 4.6 cent heavy weight discount be extended to First-Class letters weighing between 1 and 2 ounces. As discussed below, this change will help to eliminate an anomaly in the existing rate structure that provides financial incentives for mailers to take actions that make no operational sense and do not benefit the Postal Service.

Table 1 compares MMA's proposals with those of the Postal Service.

Table 1
Comparison of USPS and MMA Proposed First Class Rates
(Cents)

First-Class Category	USPS Proposed Rates		MMA Proposed Rates	
	Discount	First Ounce	Discount	First Ounce
Single Piece		34.0		34.0
Non-Automation	2.0	32.0	2.0	32.0
Basic Automation	6.0	28.0	6.2	27.8
3-Digit Automation	0.9	27.1	1.2	26.6
5-Digit Automation	1.8	25.3	1.8	24.8
Carrier Route	0.5	24.8	0.5	24.3
Heavy Weight Discount		4.6*		4.6**

*Applies to letters weighing over 2 ounces

**Applies to letters weighing over 1 ounce

3 MMA is also proposing that the Commission recognize and give presort mailers credit in the form of higher discounts for the cost sparing efforts in connection with the dissemination of automation compatible, prebarcoded courtesy envelopes and the successful implementation of the Postal Service's Move Update Program. TR 26/12297-99.

Argument

I. First-Class Rates Are Too High And Need To Be Reduced

One of the Commission's most important long term goals has been to foster and maintain a "equilibrium condition" for the First-Class revenue target. The Commission has often noted its intention to recommend rates for First Class and Standard Mail (A) that result in markup indices near the system wide average. However, since the omnibus rate proceeding in Docket No. R84-1, the Postal Service has recommended First-Class rates that were higher than they should be. As the Commission stated in Docket No. R87-1:

We have chosen to recommend First-Class rates which produce a greater contribution towards institutional costs than would have been generated by our target First-Class coverage

Our decision to recommend rates which result in coverage for First-Class which is somewhat above the average should be recognized as a one time variation from the historic, near average level we continue to believe best reflects the policies of the Act. In future cases we expect First-Class to return to that traditional level.

Postal Rate and Fee Changes, 1987, Opinion And Recommended Decision ("Op."), issued March 4, 1988, at 400, footnote 14. As the Commission stated in the next omnibus rate proceeding, Docket No. R90-1:

This is the second consecutive case in which we might have raised First-Class rates less, and raised third-class rates more, but for the potential impact of such increases on third-class mailers. Thus, despite our rate adjustments, the situation in which First-Class mailers are providing revenues which more properly should be provided by third-class mailers is perpetuated. We must comment that the choice between unduly burdening First-Class business and personal correspondence and imposing even greater percentage rate increases on businesses which rely on third-class for essential services is particularly difficult, and the Postal Service and mailers should be aware that the current status is consistent with the Act only as a short-term remedy.

Postal Rate and Fee Changes, 1990, Opinion And Recommended Decision, issued January 4, 1991, at IV-33-4, footnote 16. The Commission was forced to make the same tough choice in Docket R94-1 as well:

[T]he other consequence of implementing [a reduced First-class rate] in this case would have included average rate increases of 17 percent for

third-class, 24 percent for second-class regular rate, and even greater increases for the parcel subclasses in fourth-class mail . . . Rate increases of these magnitudes would cause the Commission serious concern about their effects upon mailers...The Commission regards [its] pricing recommendations as compromises, but compromises that are appropriate in view of the extraordinary considerations in operation here.

Postal Rate and Fee Changes, 1994, Opinion And Recommended Decision, issued November 30, 1994, at IV-16. The Commission confronted essentially the same basic issues again when it addressed the Postal Service's classification reform proposals in Docket No. MC95-1:

The Commission has expressed its reluctance to shift too large a share of the total institutional cost burden to First-Class in several recent omnibus rate cases. The Commission's willingness to establish an additional subclass within Standard Mail should not be interpreted as a retreat from the view that the largest volume subclasses in First-Class and Standard Mail should have roughly equivalent markup indices.

Mail Classification Schedule, 1995 (Classification Reform I), Opinion And Recommended Decision, issued January 26, 1996, at I-8 (citations omitted).

The Docket No. R97-1 omnibus rate proceeding again presented the Commission with the same basic issues but this time the situation was complicated by the fact that the additional revenues requested by the Postal Service were much lower than usual. Initially, the Commission's was inclined to keep the First-Class single piece rate at 32 cents; ultimately, however, it found that holding the line on the First-Class rate could not be accomplished "without imposing undue rate increases on other classes of mail." *Postal Rate and Fee Changes, 1997*, Opinion And Recommended Decision, issued May 11, 1988, at 275. In order to reduce the First-Class burden, the Commission found that "some relief can be provided to mailers of First-Class by lowering the additional-ounce rate and restraining increases for workshared mail." (*Id.* at 276)

Under the Postal Service's proposals in this case the disparity in markup indices for First Class (an increase from 132.0 to 145.1) and Standard Mail (A) (a reduction from 95.8 to 75.9) will be even more pronounced. TR 26/12281-82 (Table 2). One solution for this present and growing dilemma would be for the Commission to reject the Postal Service's proposal to increase the basic First Class rate and hold the line at 33

cents for the first ounce. However, MMA has concluded that the Commission would face the same situation it faced in the last case. As Mr. Bentley testified:

The instant proceeding is not unlike Docket No. R97-1. The total amount of additional revenues requested by the Service -- \$3.6 billion -- is not exceptionally high compared to those in the past. However, rejecting the Service's proposed 1-cent hike in the First-Class single piece rate would be difficult because of the potentially adverse impact on other mailers. In the test year, First-Class volume is expected to grow to 100 billion pieces. Thus, each penny decrease in the proposed 34-cent First Class rate represents about \$1 billion of net revenue loss that would have to be made up by other classes. In other words, holding the line on the First-Class rate would mean that all other mailers would have to shoulder the burden of the entire \$3.6 billion rate increase. It appears that would be very difficult for all other mailers to do.

TR 26/12281. On balance, MMA recommends that the Commission take the same approach that it took in the last case -- accept the Postal Service's proposal for a 1-cent increase in the First-Class 1-ounce rate and a 1-cent increase in the second and subsequent ounce rates, but lower the First-Class revenue burden by allowing workshared letters weighing between 1 and 2 ounces to receive the 4.6 cent heavy weight discount and providing for the modest increases in the discounts for workshared letters. As to the latter proposal, MMA recommends modest increases of **at least** 0.2 cents and 0.3 cents, respectively, in the Basic Automation and 3-Digit Automation discounts.⁴

II. First-Class Workshare Discounts Should Be Increased, Not Effectively Reduced As The Postal Service Proposes

As noted above, the Postal Service proposes to maintain discounts for most of the presort categories at their current levels. Under the circumstances, maintaining presort discounts unchanged effectively results in a *de facto* reduction in those discounts in real terms. As explained below, workshare discounts should be increased.

A. The Importance Of First-Class Workshare Mail

First-Class workshare mail is the most important mail category both in terms of its contribution to institutional costs and maintenance of financially viable and efficient

⁴ MMA takes no position on the proposed reduction in the discount for non-automation presorted mail.

postal services. While these presort letters incur just over one-third of the volume variable costs as First-Class single piece letters do, they contribute almost as much to institutional costs. In this regard, OCA witness Callow stresses the already heavy and increasing institutional cost burden borne by First Class mailers as a whole. TR 22/10104-10113. Mr. Callow's point is valid. Nevertheless, his presentation and graphs tend to mask the facts as they apply to workshare mail. In response to an MMA interrogatory, Mr. Callow provided similar graphs that disaggregate single piece and workshare mail. TR 22/10195-99. Those graphs show that, by any relevant measure, including average cost coverage, mark-up indices, and cost coverage indices, workshare mail shoulders the heaviest institutional cost burden.

As Table 2 shows, under the Service's proposal, presort letters, which account for only 12% of the volume variable costs, will have a **244%** cost coverage, and contribute to recovery of 32% of the total institutional cost burden. This highly efficient mail also contributes 7% per piece *more* than single piece letters to institutional costs, and about three times as much as an average Commercial Standard Mail (A) mail piece. Significantly, adoption of MMA's proposal for modest reductions in the rates for First-Class workshare letters, will change these comparisons very little.⁵

Table 2
Comparison of Test Year Finances at USPS Proposed Rates

Rate Category	% of Volume Variable Cost	% of Contribution to Inst. Cost	Cost Coverage	Unit Contribution to Inst. Cost
FC Single Piece	33%	34%	156%	\$ 0.1555
FC Workshare	12%	32%	244%	\$ 0.1667
Total First-Class	45%	66%	180%	\$ 0.1608
Commercial Std Mail (A)	23%	17%	142%	\$ 0.0568

Source: TR 26/12282

5 TR 26/12322.

Characterized by consistently strong volume growth, First-Class presort mail has demonstrated itself to be a workhorse for the postal system. The Postal Service has spent **billions** of dollars deploying automated barcoding and sorting equipment to accomplish what presort mailers do, day in and day out. Yet, according to USPS witness Kingsley, the Service's barcoding equipment is already operating at full capacity **even though the Service barcodes just 25.6% of all letters while presort mailers continue to prebarcode the lion's share -- 74.4%.** TR 5/1693; USPS-T-10 at 8. The 25% of the mail that the Postal Service's equipment does barcode is far less than the 40% the Postal Service originally anticipated (TR 26/12286; USPS-T-10 at 8, fn 5).

There is no likelihood that this situation will change in the foreseeable future. If anything, the 25% barcoding coverage factor is likely to be lower in the future. As Mr. Bentley explained, with stagnant First-Class single piece volumes and growing volumes within both First-Class and Standard Mail (A) automation categories, the percentage of letters to be barcoded by the Postal Service in the test year will tend to go down even more. TR 26/12286.

Based on the Postal Service's position that workshare discounts should be left at existing levels, one might assume that the Postal Service no longer needs to provide reasonable incentives to workshare mailers **and** stands ready to process all mail that reverts to single piece status. Such an assumption would be incorrect. As Postal Service witnesses concede, the Postal Service would experience *serious* operational problems if large portions of workshare mail reverted back to the Postal Service for barcoding and sorting. As Mr. Bentley explained in response to a question from Commissioner LeBlanc

The Postal Service's long-range, so it seems, objective here has to shrink discounts rather than increase them, and that is part of the problem I see here.

Of course, they are stuck. They can't really decrease [workshare discounts] very much because they would be in very big trouble now if some of this mail decided to revert back to single piece. I think there have been some rumblings to that effect because of the problems that some of the mailers, at least the members of MMA, are having with the Postal Service's non-uniform administration of the preparation requirements.

So down the road it appears to me that the Postal Service is going to have to remain competitive and if they want to keep the volume in there they

This is not the first time the Postal Service has proposed to raise workshare mailers rates by increasing the basic First-Class rate while leaving workshare discounts at current levels. Nor is it the first time that a postal official has warned workshare mailers of anticipated future reductions in discounts. A decade ago, USPS witness Ashley Lyons issued a similar cautionary warning to mailers. As the Commission noted in its Opinion And Recommended Decision in Docket No. R90-1,

With greater automation and corresponding processing cost reductions, the Service argues that the value of mailer presortation to the Postal Service is anticipated to decline. Witness Lyons states that offering further incentives to presort mailers "sends a confusing signal as it overshadows automation-related worksharing. This anticipated reduced role for presorted mail is reflected in the Service's proposal to keep the presort discounts at the Docket No. R84-1 and R87-1 level of four cents.

Op. R90-1 at V-27. The Commission did not heed witness Lyon's warning in that case. Instead of leaving the discount at 4.0 cents, as the Service recommended, the Commission recommended increasing the discount to 4.2 cents. *Id.* at V-48, 50.

The Service's predictions in 1990 that the value of workshared mail to the Service would decline due to the introduction of more automated equipment, and that there would be a reduced role for presort mailers, proved wrong. In fact, just the opposite is true. In the intervening years, properly measured workshare cost savings and the discounts have increased, as witness Fronk recognized (TR 12/4873)⁷. If anything, presort mailers have played an increasingly pivotal role in assuring the financial success of the Postal Service, and, despite a very ambitious automation program during the intervening decade, today the Postal Service must rely more than ever on workshare mailers to accomplish its vital mission.

For these reasons, the Commission should look very skeptically at Postal Service warnings that the value of worksharing to the Postal Service could/might/may

⁷ Nor has the value of worksharing declined over the past decade. Time series cost data for presort and nonpresort letters indicate that, over the past 10 years, unit costs in constant dollars have decreased about the same amount, as USPS witness Fronk confirmed (TR 12/4872-73). See Order 1289, issued March 28, 2000. Attachment A at 2.

be declining.⁸ As discussed in the following section, the Commission should also be critical of apples and oranges comparisons of workshare cost savings that the Service has offered in support of such warnings.

C. The Postal Service's Measurement Of Workshare Cost Savings Is Flawed

The following table compares the Postal Service's First-Class presort cost savings and the proposed discounts in this case with those of the Commission in Docket No. R97-1:

Table 3
Comparison of First-Class Presorted Cost Savings
And Proposed Discounts⁹
(Cents)

First-Class Category	PRC Docket No. R97-1		USPS Docket No. R00-1	
	Cost Savings	Discount	Cost Savings	Discount
Basic Automation	7.2	6.0	4.9	6.0
3-Digit Automation	0.9	0.9	1.0	0.9
5-Digit Automation	1.8	1.8	1.2	1.8
Carrier Route	0.5	0.5	0.3	0.5

If the Postal Service's measurement of the workshare cost savings is to be believed, those savings have plunged dramatically, from 7.2 cents in Docket No. R97-1 to 4.9 cents. In view of this "evidence," it is frankly incredible that USPS witness Fronk could recommend that existing discounts be maintained.

The Commission need not concern itself with the Postal Service's finding that the related cost savings are lower than the workshare discounts the Service is proposing. The unit cost savings that the Postal Service derives for workshare letters in this case

⁸ At the same time that USPS witness Fronk warns First-Class mailers that the "value of presorting to the Postal Service" may have "peaked", he also has stated that, "I have not alleged that the value of worksharing to the Postal Service has peaked." See TR 12/4730.

⁹ Sources for the costs and discounts shown in Table 2 are as follows: Op. R97-1 at 297, USPS-T-24 at 18.

simply are not comparable to the cost savings derived by the Commission in the last case. As Mr. Bentley explains "the Postal Service's derived workshare cost savings are, indeed, lower than those derived in the last proceeding; but only because the Service's new methodology *insures* that they will be lower. TR 26/12287 (emphasis in original).¹⁰

1. Differences Due To The Service's Change In Basic Costing Methodology

One of the most important methodological changes proposed by the Service involves the claim that labor costs do not vary 100 percent with volume. Mr. Bentley counsels against rejection of the Commission's longstanding position that labor costs vary 100% with volume and adoption of the Postal Service's new cost attribution methodology. As he points out, attributing costs on the assumption that labor costs do not vary 100 percent with volume reduces the amount of total costs considered attributable, a reduction of \$3.5 billion in this case, and increases the amount of such costs that are considered to be "institutional" costs. Ultimately, such a change in cost attribution methodology will, more than likely, result in the assignment of an excessive portion of institutional costs to First-Class Mail.¹¹ Such a change in cost attribution methodology would also artificially reduce derived workshare cost savings and mask the traditional yardsticks used by the Commission to judge the fairness of proposed rates. TR 26/12290.

2. Arbitrary Exclusion Of Relevant Costs From The Measurement Of Workshare Cost Savings

In this case, the USPS witness Miller proposes another significant change in the methodology for measuring workshare cost savings. He removed from his analysis of workshare cost savings of over 1.3 cents in 22 MODS cost pools because he deemed

10 For example, Mr. Bentley demonstrates that the new cost attribution method proposed by the Postal Service and employed by USPS witness Miller has the effect of reducing workshare cost savings. TR 26/12290-91 (Table 8).

11 As discussed below, the Postal Service's attribution of updated costs to reflect FY 1999 as the base year in response to Commission Order 1294 is significantly biased against First Class. The Postal Service has a long history of attempting to "assign" First Class an excessive portion of institutional costs in order to benefit Commercial Standard mailers.

the costs to be unrelated to worksharing. Excluding these costs from consideration had the effect of reducing Basic Automation cost savings by .63 cents and reduced the savings from 3- and 5-Digit Automation letters by 30 percent. TR 26/12291.

There are several very obvious problems with Mr. Miller's narrow definition of cost savings. First there is the problem of possible sampling errors that result due to the loss of accuracy that accompanies the disaggregation of cost data to very low levels. TR 26/12291-92. Second, the cost pools that USPS witness Miller proposes to exclude do not affect single piece and workshare letters in the same manner. As Mr. Bentley observes, "in virtually every case, workshare letters cost less than single piece letters." *Id.* The fact that USPS witness Miller cannot explain the cost differences is a "fundamental flaw"¹² in the Postal Service's case. As Mr. Bentley elaborated:

If exogenous factors impact single piece letters and workshare letters differently, then Mr. Miller's CRA- and model-derived unit costs do not accurately reflect just workshare cost differences, his stated goal. In other words, eliminating the cost pools Mr. Miller removed essentially invalidates his derived workshare cost savings.

However, if the exogenous factors impact single piece and workshare letters similarly, which I contend, then the observed cost differences totaling over 1.3 cents in the cost pools that Mr. Miller removed from consideration are more than likely caused by worksharing attributes. Accordingly, they should be included in, not eliminated from, the workshare cost savings analysis.

In either situation, inclusion of these cost pools in the analysis will produce a more accurate estimate of workshare cost savings. If particular costs are unrelated to worksharing, as Mr. Miller claims, and the costs affect single piece and workshare letters alike, then including the cost pools in the analysis will have no impact on the derived cost differences.

TR 26/12293. See also TR 26/12362-64. Moreover, Mr. Miller's "judgments" on excluding these cost pools from consideration are at odds with the judgments made by Postal Service witness in other cases. USPS witness Hatfield, who testified proceeding, chose to include such cost differences as part of the presort cost savings derivation. Therefore, the purely precatory statements Mr. Miller chose to rely upon are irrelevant, since witness Hatfield made no reduction in the measured cost savings. In

12 TR 26/12292.

Docket No. MC95-1, USPS witness Smith actually went one step further by specifically concluding that platform costs (among others) "are, in fact, presort related". Docket No. MC95-1 at IV-44 and IV-31.¹³

Since USPS witness Miller proposes to eliminate from consideration mail preparation, platform and other cost pools in his derivation of workshare cost savings, the Postal Service must bear the burden of proof on this issue. The Service did not even begin to meet that burden. Mr. Miller's failure to explain why platform costs are different is remarkable, particularly because he claims that the differences are due to factors other than worksharing but performed no study. TR 7/3176-77. In fact, he has no idea what mailers do in order to facilitate the movement of presorted letters within and between post offices. Mr. Miller is no expert on how presort mailers prepare their mail, as he conceded repeatedly:¹⁴

I am not really an expert on presort mailers so I wouldn't know the answer to questions in terms of what they do prior to entering their mail at a postal facility.

TR 7/3149.

It is **inconceivable** that the Postal Service witness responsible for deriving workshare cost savings, affecting billions of dollars, does not know, or understand what worksharing activities are performed by mailers before the mail is provided to the Postal Service. What is even more astounding to MMA and should be to the Commission is how, without any knowledge of such activities, Mr. Miller had the temerity to unilaterally declare, categorically, that mail preparation activities are "unrelated to worksharing."

The record demonstrates that mail preparation activities do not include only traying of mail, as Mr. Miller was led to believe, but much, **much** more. As this record shows beyond question, these extensive mail preparation activities are very expensive

13 See also TR 44/19087, fn 2. MMA witness Harrison specifically points out that palletizing as well as other mail preparation requirements serve to reduce platform costs. TR 26/12245-50.

14 Mr. Miller confessed "I'm not really sure what the specific palletizing requirements would be, "I'm not really aware of what the specific requirements are for [stretch-wrapping] pallets," he did not know if the mailers were required to sort the pallets, did not know whether mailers are required to place ACT or D&R tags on the pallets, and did not even know what a D & R tag was. TR 45/19774. Then he admitted again, "I'm not really an expert on mail prep requirements." *Id.*

for the mailers. And, notwithstanding Mr. Miller's uninformed opinion, these activities certainly do impact mail preparation and platform costs. TR 44/19085-89. As Mr. Bentley testified,

Q Now, are these platform cost savings and mail cost savings, matters that have been included in worksharing cost avoidance in the past, that Witness Miller has proposed be excluded in this case?

A As a matter of fact, the platform cost savings were included in R97. He's proposing to exclude them, but there are so many factors, including all of the workshare regulations that the mailers have to comply with, just in designing the piece. Then they face and pack the letters into the trays. They sleeve the trays, they have to strap the trays. This is all at their own cost. They have to label the trays. They have to add the air contract transportation tagging. Sometimes they have to add the destination routing labels. The trays are segregated and sorted, and they are then packed onto pallets and the pallets are stretch-wrapped. And then the pallets are sorted onto trucks, so, in a sense, the trucks are sorted. Now, these are all factors that BMM, as being the benchmark from which cost savings are measured, don't do. And these are all activities that will tend to reduce the platform cost handling within the Postal Service.

TR 26/12378-79.

In view of the Postal Service's failure to justify its dramatic change to the established methodology for measuring workshare cost savings, Mr. Bentley urged the Commission to adopt a commonsense "Rule Of Reason" approach – "When in doubt . . . leave costs in the analysis. If the cost pools are not affected by worksharing, and the cost pools are accurate, then leaving the costs in the analysis will not impact the final results." TR 26/12294. Responding to the Service's suggestion that this course could overstate worksharing related savings, Mr. Bentley confirmed that "leaving in costs that affect each of the First-Class categories in the same manner will not overstate the worksharing related savings" and "if the costs at the cost pool level are not very accurate, as I believe could be the case, then there would be no harm in leaving such costs in since doing so will not change the derived workshare cost savings if, as Mr. Miller maintains, platform costs are not affected by worksharing." TR 26/12363-64.

Application of these logical principles alone would warrant rejection of Mr. Miller's novel proposal to eliminate significant cost differences from the measurement of workshare cost savings. But the record now contains substantial evidence demonstrating affirmatively why it would not be proper to exclude these cost differences from consideration. In response to Postal Service interrogatories MMA witnesses Harrison and Bentley discussed the First-Class workshare mail preparation regulations as they currently exist and are administered. See TR 26/12240-41, 12246-12250, 12370-72. Their testimony demonstrates beyond question that in order to qualify for First-Class automation discounts, workshare mailers must comply with a vast array of prerequisite requirements relating to design of the mailing piece itself and to preparation of letters prior to the time they are deposited with the Postal Service.

The costs in question must be borne by the mailers and mailers are not given proper credit for these activities that benefit the Postal Service directly. As Mr. Bentley testified:

All of the costs associated with such activities are borne by workshare mailers. While the Postal Service's analysis indirectly considers cost savings that result from mail piece design activities, it totally disregards cost savings resulting from mail preparation activities. The reason for this is simple: USPS witness Miller's derivation of workshare costs savings does not consider mail preparation or platform activities to be workshare-related.

TR 44/19085-86 (emphasis added). Mr. Bentley's analysis includes mail preparation and platform cost savings totaling \$442 million, equivalent to just under 1.0 cent per piece, that USPS witness Miller's analysis excluded. TR 44/19086, 19094. However, even Mr. Bentley's method for measuring workshare cost savings does not give mailers adequate recognition and credit for these beneficial activities:

[N]ot all of the mail preparation cost savings have been properly isolated or analyzed by the Postal Service. I am referring to cost savings that the Postal Service will realize by "requiring" workshare mailers to perform mail preparation tasks that postal workers performed in the Base Year but no will longer perform by the Test Year.¹⁵ To the extent such transfers of

15 In response to Interrogatory USPS/MMA-T2-5(b) I stated that, "MMA mailers are continually negotiating with local postal officials, who keep on placing (and shifting) more cost burdens upon them." Two examples of these activities are attaching ACT Tags and D&R labels to trays. See TR 26/12379-80.

cost responsibility for mail preparation activities are not captured by the Postal Service's roll-forward model, postal costs for workshare letters will be overstated and workshare cost savings will be understated.

TR 44/19086.¹⁶ In order to remedy this inequitable state of affairs, MMA recommends that the Commission direct the Postal Service to measure the cost impact of workshare mailers' compliance with qualifying regulations, and to include such savings as part of its derived cost savings in the *next* omnibus rate proceeding. That does not mean, however, that the Commission should totally ignore the importance of these hidden cost savings in this case. The Postal Service must accept some responsibility for the lack of record evidence on this subject. After all, it was the Postal Service who appointed Mr. Miller, the witness who did not know how workshared mail is prepared and handled prior to the time it enters the postal system. Accordingly, in considering how much the existing discounts should be increased by, the Commission can and should give substantial weight to the testimony of Mr. Bentley and Ms. Harrison on the cost sparing benefits that accrue to the Postal Service as a result of these hidden worksharing activities.

3. Use Of An Unrealistic, Inappropriate Benchmark For Measuring Savings

Still another problem with the Postal Service's measurement of workshare cost savings lies in the use of an unrealistic benchmark from which to measure cost savings. In Docket No. R97-1, the Commission accepted Bulk Metered Mail ("BMM") as the appropriate benchmark and that is what the Postal Service *claims*¹⁷ to have used in

Of course, transferring the costs for such activities from the Postal Service to mailers will not show up as part of workshare cost savings in either Mr. Miller's analysis or Mr. Bentley's analysis. TR 44/19086.

16 Mr. Bentley identified requirements that workshare mailers attach ACT Tags and D&R labels to trays as but two examples of how local postal officials have been shifting more of their cost burdens to mailers. TR 44/19086, fn 1. Mr. Bentley also testified that "[t]ransferring the costs for such activities from the Postal Service to mailers will not show up as part of workshare cost savings in either Mr. Miller's analysis or my analysis." *Id.*

17 In the final analysis, the choice of a benchmark has no effect whatsoever on the outcome of Mr. Miller's workshare cost analysis, as he confirmed during cross examination. TR 45/19770-71. In other words, under Mr. Miller's methodology, it makes no difference what benchmark mail (e.g. BMM or MML) is used.

this case.¹⁸ In fact, Mr. Miller's benchmark is a nonprebarcoded, nonpresorted automation-compatible letter that meets all the prerequisite design and the mail preparation regulations that current First-Class Automation mail must meet, including Move Update and reply mail requirements. MMA contends that no such mail exists in the current mail stream, it never has, and it never will.

MMA urges the Commission to reconsider use of BMM and instead adopt Metered Mail Letters ("MML"). Using MML rather than BMM as the benchmark simply recognizes that mail preparation costs are also avoided by worksharing efforts of presort mailers.

Mr. Bentley explains how choice of an appropriate benchmark mail piece relates to the process of deriving workshare cost savings:

The objective of the cost savings analysis is to isolate costs that the Postal Service can avoid when mailers presort and prebarcode their own letters. In other words, benchmark letters should represent what workshared letters would be if they were not prebarcoded or presorted.

TR 26/12294. There is more to presorting and prebarcoding than meets the eye, which is why the Postal Service has established a myriad of additional regulations that further defines and refines the workshare criteria.

Using BMM as the benchmark assumes that the letters are always properly faced, trayed, and brought to the post office for mailing. The Postal Service has failed to demonstrate that such an assumption is reasonable, let alone accurate. Mr. Bentley explains at length why using BMM as the benchmark is unrealistic and unfair to presort mailers. The Postal Service witnesses who advocate using BMM as the benchmark do not agree on why they chose BMM and merely *assume* that BMM is still the mail most likely to convert to workshare status; neither they nor the Postal Service have any reliable data demonstrating that BMM even exists in today's mail stream.

Unlike the Postal Service witnesses, Mr. Bentley traces the evolution and maturation of the presort program and explains how the characteristics of the type of mail most likely to convert to worksharing has changed over time. TR 26/12295-96. He

¹⁸ Mr. Bentley provides a concise review of the benchmarks utilized by the Commission over the years. TR 26/12315.

also explains why it is illogical to assume that mailers will forego workshare discounts but still voluntarily prepare their mailings in the same manner as presort mailers and why, even assuming some small number of isolated mailers do so, it is unfair to penalize all workshare mailers who mail out 47 *billion* pieces per year.

Perhaps stung by Mr. Bentley's and Mr. Clifton's criticisms of the Postal Service's use of an essentially imaginary benchmark, in rebuttal testimony Mr. Miller claimed to have discovered the mother lode of BMM – some 14.7 *billion* pieces. TR 45/19649. This came as quite a surprise to MMA. Despite MMA's best efforts to obtain volume and other relevant information about BMM through discovery, the reports of BMM sightings were rarer than those for the Loch Ness monster. TR 21/8903-4; TR 26/12365-66.

As it turns out, Mr. Miller's mother lode probably is fools' gold, not the real thing. First, the total volume of Metered Mail letters, of which BMM is a subset, shown by Mr. Miller (28.9 billion pieces) exceeds by a wide margin the next nearest measure of Metered Mail letters (19.7 billion as shown in USPS-LR-416 (Table 10B)). Second, as Mr. Miller admitted, the volumes he shows are not really machine counts. Instead, the volume figures are derived from an undisclosed weight conversion formula that makes assumptions (apparently erroneous) about the average weight of pieces of all types. TR 45/19698. Third, although Mr. Miller labeled the entire 14.67 billion pieces as BMM (TR 45/19649), he admitted "[s]ome of this mail – by saying in parentheses that this is where the BMM is, ***some of this mail is not actually what we would probably be defining as BMM.***" TR 45/19699 (emphasis added). It turns out that some unknown portion consists of flats, some additional (also unknown) portion is standard mail (TR 45/19702), and some additional portion (perhaps most) represents metered mail that the mailer originally placed into local collection boxes, either separately or in bundles, and postal workers later trayed. TR 45/19699-19701). Individual mailings of metered letters, trayed by postal workers or window clerks could hardly be defined as "bulk", in the context of BMM. Finally, Mr. Miller's story makes no sense. If there were truly 14 billion pieces of BMM in the current mailstream, one must wonder how the presort bureau industry has failed to capture so much of its potential market over the past 23 years during which presort discounts have existed.

In the end, Mr. Miller's story about the existence of BMM ends at the same place the record stood after the Postal Service was asked discovery questions about BMM. Ultimately, the Commission will have to judge the credibility of Mr. Miller's story about the existence of BMM. MMA's only parting observation is that stories that sound too good to be true often are.

4. Failure To Consider Other Cost Sparing Attributes Of Presort Letters

The methodology that the Postal Service employs to derive workshare cost savings also arbitrarily excludes from consideration other cost sparing attributes of presorted letters. These include prebarcode savings of .46 cents per originating letter resulting from a Postal Service requirement that courtesy reply envelopes enclosed in outgoing workshare letters must meet automation compatibility requirements and be prebarcoded, savings of almost .9 cents per originating workshare letter that is attributable to reduction in the proportion of mail requiring forwarding or return service that has occurred due to presort mailers' compliance with the Service's Move Update Program, and window service cost savings of about 1.5 cents. TR 26/12297-99. MMA witness Sharon Harrison provides further support for giving presort mailers appropriate credit in the determination of presort discounts for a portion of the savings achieved due to presort mailers support for prebarcoding CEM letters and their contributions to the successful Move Update Program. TR 26/12221, 12224-29,¹⁹

C. MMA's Proposal For Modest Increases In Presort Discounts Are Reasonable

Reproduced below are two tables from MMA witness Bentley's testimony. TR 26/12300. Table 4 shows the total cost savings and workshare-related cost savings derived by Mr. Bentley and the presort discounts he recommends in this case. As

¹⁹ This testimony demonstrates the substantial commitments of time and expense that workshare have made and continue to make to insure success of the Move Update Program. It also demonstrates that mailers such as SBC often go the extra mile in terms of implementing more often address updates to reduce Undeliverable As Addressed mail. TR 26/12221. Finally, as Ms. Harrison knows first hand the notion that UAA errors and return mail problems are caused by mailers is a myth. In a study that Ms. Harrison's company conducted with the Postal Service, the USPS was responsible for 22% of errors in handling returned mail as compared to the 7% of errors attributable to the company. TR 26/12231.

Table 3 shows, Mr. Bentley proposes to increase the discount for Basic Automation Letters by 0.2 cents to 6.2 cents, and to increase the discounts for 3-Digit and 5-Digit Automation Letters by 0.3 cents.

Table 4
MMA Proposed First-Class Workshare Discounts
(Cents)

First-Class Category	Total Cost Savings	Workshare-Related Cost Savings	Current Discount	MMA Proposed Discount
Basic Automation	9.7	6.9	6.0	6.2
3-Digit Automation	4.3	1.5	0.9	1.2
5-Digit Automation	4.7	1.9	1.8	1.8
Carrier Route	3.3	0.5	0.5	0.5
Source: MMA-LR-1				

Table 5 shows the resulting presort rates and the percentage increases.

Table 5
Comparison of Current and MMA Proposed First-Class Rates
(Cents)

First-Class Category	Current Rate	MMA Proposed Rate	MMA Proposed Increase
Single Piece	33.0	34.0	3.0%
Basic Automation	27.0	27.8	3.0%
3-Digit Automation	26.1	26.6	1.9%
5-Digit Automation	24.3	24.8	2.1%
Carrier Route	23.8	24.3	2.1%

The discounts derived by Mr. Bentley do not include (1) additional cost savings related to enclosure of prebarcoded CEM envelopes in workshare mail pieces, (2) presort mailers' contributions to the success of the Postal Service's Move Update Programs, and (3) credit for window service costs that workshare mail by definition does not incur. As discussed below, such items represent real savings to the Postal Service

that the Commission can and should consider in determining the appropriate level of workshare discounts.

1. Savings Achieved By Enclosed Prebarcoded Reply Envelopes

Courtesy reply envelopes enclosed in an outgoing workshared letter must meet certain automation compatibility requirements and be prebarcoded. When returned, these envelopes present a cost savings opportunity to the Service since they can bypass the entire RBCS (barcoding) operation. Such mail saves the Postal Service almost 4 cents per piece. TR 29/14010.

The current rate structure gives workshare mailers no credit for the prebarcode savings these reply envelopes confer on the postal system. Mr. Bentley estimated the total test year cost savings due to prebarcoded letters sent out at First-Class Automated rates and returned at Single Piece rates at \$205 million, equivalent to .46 cents per originating First-Class automation letter. TR 26/12297-98; Library Reference MMA-LR-1 at 45. MMA urges the Commission to give presort mailers the credit they are entitled to for preparing these very efficient, cost sparing reply mail pieces.

2. Savings From Compliance With Postal Service Move Update Requirements

In recent years, the Postal Service has implemented several new programs to ensure the accuracy of addresses. MMA witness Sharon Harrison, who has extensive experience with such matters and has led an award winning joint USPS/Pacific Bell study of UAA problems, provided details regarding the Postal Service's requirements for address cleansing, and specifics of the education, time, and expense that workshare mailers incur to meet and remain in compliance with all applicable programs and requirements. TR 26/12219, 12221-23, 12224-26, 12230-32.

A recent Postal Service study reported that the move update programs are working and saved more than \$1.5 billion in forwarding and return costs in FY 98 alone.

Library Reference USPS-LR-I-82 ("1998 UAA Study"). That study also indicated that move update programs **significantly** reduced the proportion of mail requiring forwarding or return service, **from 5.39% to 2.73%**. See TR 21/8896-99; TR 26/122298. As Mr. Bentley testified "[t]hese figures indicate that move update programs have been a **smashing success**." TR 26/12298 (emphasis added).

It is entirely logical, and only fair, that First-Class presort mailers who have worked closely with the Postal Service to maximize the effectiveness and cost savings from the Move Update programs should share in those cost savings. But in this case, the Postal Service's analysis of workshare cost savings gives presort mailers absolutely **no credit** whatsoever for their significant, **ongoing** contributions to the success of the important move update programs. *Id.*

USPS witness Miller testified, in the abstract, that "[h]ad there been any additional worksharing related savings that I was unaware of that came to my attention, I would have attempted to evaluate it." TR 7/3146. He claimed he was unfamiliar with the Postal Service's 1998 UAA Study and had not studied the issue. Nevertheless, he apparently was not concerned that presort mailers, who helped the Postal Service achieve savings of more than \$1.5 billion in the base year, were not adequately compensated in any way. TR 7/3159-60, 3163, 3189.

Obviously a great deal of time, effort, and expense went into conducting a special study and having an independent consultant prepare the 1998 UAA Study. Moreover, shortly before this case was filed, the Postal Service trumpeted how good the results of the Move Update Programs were in the publication *Memo to Mailers*. TR 21/9439-40.

After the case was filed, however, the 1998 UAA Study became an orphan. Even worse, the Postal Service produced statistics which appeared to call the results of the UAA Study into question. TR 21/8907. USPS witness Pafford whom the Postal Service finally put forward after it resisted producing a witness, also sought to cast doubt on the UAA Study by comparing it unfavorably with the Service's ODIS data system (TR 21/9432, 9436) and suggesting that it should be given little weight because it was a two week special study and he did not know who had commissioned it. TR 21/9433.²⁰ Mr. Pafford, recognized, however, that special studies are often used where reliable information cannot be obtained from the general data systems, such as ODIS, available to the Postal Service. He also acknowledged that the using the ODIS system

20 In fact, the UAA Study was commissioned by the Postal Service Office of Address Management at the National Customer Support Center in Memphis, Tennessee, which Mr. Pafford agreed "is sort of the national headquarters" for address management issues. TR 21/9435.

to provide this type of data was "relatively new" and he had not determined how reliable the ODIS data was. TR 21/9429, 9436.

Despite the Postal Service's efforts to distance itself from the superlative results reported in its own UAA Study, the fact remains that the study is the best, most reliable evidence of the substantial cost savings benefits the Postal Service has enjoyed as a result of workshare mailers compliance with Move Update requirements. It also provides a sound basis for giving workshare mailers some well deserved dollars and cents credit for their contributions to the success of these programs.

Based upon the percentage reduction in letters that require forwarding and return service, Mr. Bentley calculated that savings of almost 0.9 cents per originating workshared letter should be added to derived unit workshare cost savings. See Library Reference MMA-LR-1 at 43. MMA urges the Commission to take these important cost sparing efforts of presort mailers into account when determining the specific level of presort discounts it will recommend now and in the future.

3. Averted Window Service Costs

Many First-Class single piece mailers purchase postage and deposit their mail at a post office window. Presort mailers do not do so. Providing window service costs the Postal Service well over \$700 million per year, equivalent on average, to about 1.5 cents for each single piece letter. TR 26/12299. Such costs are built into the basic First-Class rate but are not reflected in the discounts presort mailers receive. Mr. Bentley recommends that the Commission consider them in a qualitative sense when determining the appropriate discounts for presort mail categories. *Id.*

The modest increases in presort discounts that MMA is proposing are lower than the derived cost savings, and much lower than the total cost savings that presort mailers should receive credit for. The high cost coverage for First-Class as a whole and the much higher implicit cost coverage for presort letters warrants even greater increases in the discounts. However, limiting increases in the workshare discounts at this time insures that there will be no adverse impact on the Service's proposed rates for other subclasses and services.

III. Issues Regarding The First Class Additional Ounce Rate

In this case, the Postal Service proposes to raise the additional ounce rate for First-Class mail from 22 cents to 23 cents per ounce. In part to support that proposal, USPS witness Daniel prepared and presented the results of a study that purported to measure the impact of weight on costs.

The Daniel weight study does not provide reliable information regarding the *isolated* impact on processing costs of the second ounce of a two-ounce letter. Notwithstanding USPS witness Fronk's and Daniel's initial testimony to the contrary, Mr. Bentley testified, "this study still fails to address the Commission's desire for reliable information regarding the specific cost impact of the second ounce of a letter." TR 26/12303; TR 4/1255, TR 12/4751. The problem is that Ms. Daniel studied each ounce increment as a completely separate entity and attributed volume variable costs on the basis of various distribution keys. In doing so, Ms Daniel treated each ounce increment in a fashion usually reserved for subclasses, such that the resulting cost differences reflect *all* of the relevant cost attributes²¹ (in addition to weight). TR 26/12303. Accordingly, the cost differences among the weight increments found by the Daniel Study are not caused by weight and it is totally improper to conclude, as USPS First-Class rate witness Fronk apparently did (see TR 26/12354-55), that a 2-ounce letter costs more than a 1-ounce letter "*solely because they weigh more*" (TR 26/12304).

USPS witness Daniel subsequently changed her position about meeting the Commission's long term goal of measuring the impact of weight on cost. In response to an MMA interrogatory she agreed that "[t]he cost study reflects all the characteristics associated with the average piece in each weight increment" and that "since [her studies] do not completely isolate for the impact of weight, they do not provide the 'specific impact of weight on costs'" TR 4/1262; TR 26/12303.

²¹ Such cost-causing attributes include (1) local/nonlocal mix, (2) origin/ destination pattern, (3) degree of presortation, (4) prebarcode vs. no prebarcode, (5) machinability, (6) delivery to a p.o. box vs. delivery by carrier, (7) likelihood of being undeliverable-as-addressed, and (8) likelihood of being barcoded. TR 26/12303.

MMA proposes the 4.6-cent heavy weight discount that currently applies to letters weighing over 2 ounces be applied to automation letters weighing between 1 and 2 ounces. Adoption of MMA's proposal would not disturb the Commission's preference for a uniform rate structure for additional ounces. It would also be consistent with USPS witness Fronk's observation "that initial additional ounces cost less for presort, but that this difference does not continue to grow as the pieces get heavier." USPS-T-33 at 31. In addition, as Mr. Bentley elaborated in response to a question from Commissioner Omas,

I can sit here today and say to you it is reasonable to assume that if a letter weighing two ounces goes through a piece of machinery and gets sorted the same as a one ounce piece there is no additional cost between processing those two pieces.

TR 26/12376-77. It simply seems implausible that after 13 years the Postal Service is unable to disprove and unwilling to admit the obvious truth: 2-ounce letters cost no more to process than 1-ounce letters. The Service maintains a Standard Mail rate structure that implies this fact and encourages mailers to add weight to their mailing pieces (up to 3.3 ounces) without additional cost. Moreover, in its cost models the Postal Service utilizes the same productivity figures for processing First-Class and Standard Mail letters even though, on average, the Standard Mail letters weigh significantly more. As Mr. Bentley continued in response to Commissioner Omas' inquiry:

I have been looking at the data for a period of at least these 13 years and I would venture to say the only additional cost that is weight-related has to do with transportation and that is **on the order of magnitude of a penny or less**, so in my view the additional cost to process a two ounce letter versus a one ounce letter is about a penny when they are charging 22 cents, so that to me is a **very large** cross-subsidization of two ounce letters to one ounce letters. It is a disproportionately high charge to cover the cost that is incurred by that second ounce.

TR 26/12377 (emphasis added).

MMA witness Mury Salls provides additional support for implementation of the additional ounce rate recommended by Mr. Bentley. Mr. Salls explains how the existing rate structure encourages mailers to "break up" their mailings into two separate mailings

– a First-Class mailing limited to one ounce per piece and a Standard (A) mailing weighing up to 3 ounces. Mr. Salls has presented, in Exhibit MMA-3A, an illustration of how mailers save money by breaking up their mailings in this fashion. TR 26/12266-67.

Table 1 of that exhibit shows that breaking up a 10,000 piece 2-ounce mailing into two separate mailings can save a mailer approximately \$540, even though the Postal Service incurs significantly greater costs to handle and process twice the number of pieces. TR 26/12266. Table 2 (TR 26/12267) demonstrates how extending the heavy weight discount to pieces weighing between 1 and 2 ounces will help to eliminate the counterproductive incentives built into the current additional ounce rate structure and will persist under the Postal Service's First-Class rate proposals. TR 26/12264.

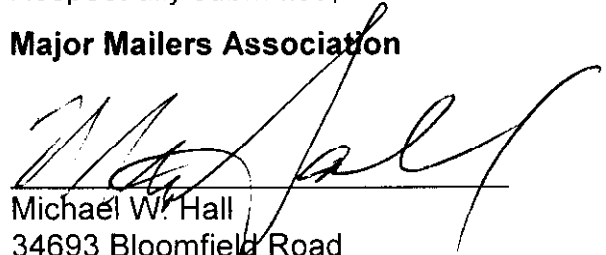
Conclusion

For the foregoing reasons, the Commission should adopt MMA's recommendations for reasonable increases in the discounts for presort mail and extension of the heavy weight discount to letters weighing between 1 and 2 ounces.

Respectfully submitted,

Major Mailers Association

By:

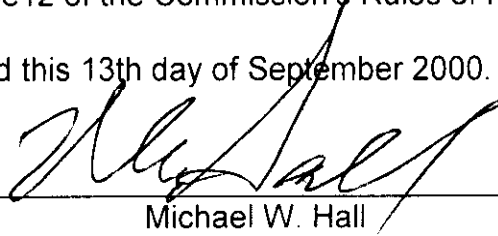

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Dated: Round Hill, VA
September 13, 2000

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all parties to this proceeding, in compliance with Rule 12 of the Commission's Rules of Practice.

Dated this 13th day of September 2000.

A handwritten signature in black ink, appearing to read "Michael W. Hall", is written over a horizontal line.

Michael W. Hall